

Message Text

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E.O. 11652:

TAGS: ENRG

SUBJECT: IEA - SLT REPORT TO GOVERNING BOARD

1. PLEASE PASS TO IEA SECRETARIAT (KELLY) FOLLOWING
SECTIONS OF SLT REPORT TO GOVERNING BOARD ON ITS MEETING
OF FEBRUARY 19-21. COVERING NOTE SHOULD EXPLAIN THAT
FIRST SECTION OF REPORT (PROS AND CONS OF POSSIBLE ELE-
MENTS OF COORDINATED SYSTEM) REPRESENTS INTENSIVE REVIEW
BY SLT OF ORIGINAL DRAFT SUMMARY OF DISCUSSION WHICH WAS
PREPARED BY SECRETARIAT WITH ASSISTANCE OF SEVERAL DELE-
GATIONS. FINAL TWO SECTIONS (PRICES AND MARKET TRENDS
AND BURDENSARING) ARE ALSO BASED ON EXTENSIVE SLT DIS-
CUSSION AND HAVE BEEN REVISED TO REFLECT COMMENTS MADE BY
DELEGATIONS. HOWEVER,THESE TWO SECTIONS DID NOT RECEIVE
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SAME INTENSIVE REVIEW BY FULL SLT AS THE FIRST PART OF THE
REPORT AND MAY NOT REPRESENT AS COMPLETE A REFLECTION
OF THE VIEWS OF DELEGATIONS AS THE FIRST SECTION.
NOTE SHOULD ALSO INDICATE THAT THIS DIFFERENCE REFLECTS

THE INSTRUCTIONS FROM THE GOVERNING BOARD THAT AT THIS STAGE IN ITS WORK THE SLT SHOULD CONCENTRATE PRIMARILY ON THOSE ASPECTS OF POSSIBLE COORDINATED SYSTEM ON WHICH GOVERNING BOARD WILL URGENTLY NEED ANALYSIS IN ORDER TO ARRIVE AT SUITABLE AGREEMENT IN PRINCIPLES AT AN EARLY DATE.

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2. PRICES AND MARKET TRENDS.

THE CONDITIONS AND TERMS UNDER WHICH POSSIBLE PRICES COULD BE RELATED TO AN EQUILIBRIUM OF INTERESTS AND RELATIONSHIPS BETWEEN THE PRODUCERS AND CONSUMERS.

A) ANY GENERAL MEASURE OF PRICE PROTECTION WHICH MIGHT BE ADOPTED BY THE IEA SHOULD BE A COMMON LEVEL OF PROTECTION FOR INVESTORS IN IEA AREAS. ANY EQUILIBRIUM PRICE THAT MAY BE NEGOTIATED BETWEEN OIL CONSUMERS AND PRODUCERS SHOULD BE IN THE INTEREST OF BOTH PRODUCERS AND CONSUMERS.

ONE DELEGATION NOTED THAT IT MIGHT BE POSSIBLE FOR THE EQUILIBRIUM PRICE TO FUNCTION AS A FLOOR PRICE IF THE FORMER COULD BE AGREED UPON AND MAINTAINED UNDER REASONABLE CONDITIONS FOR AN EXTENDED PERIOD OF TIME. IT WAS POINTED OUT, HOWEVER, THAT SUCH A DE FACTOR FLOOR PRICE MIGHT BE RELATIVELY HIGH.

B) SINCE THE TWO PRICES HAVE DIFFERENT FUNCTIONS, THEY MIGHT WELL BE FOUND AT DIFFERENT LEVELS.

C) THE TIME SCALE FOR THE TWO PRICES MIGHT BE DIFFERENT. A FLOOR PRICE SHOULD BE OF A RELATIVELY LONG DURATION SO AS TO COVER THE PERIOD NEEDED TO REALIZE A RETURN ON CAPITAL INVESTMENT, WHILE AN EQUILIBRIUM PRICE MIGHT BE ESTABLISHED FOR A SHORTER PERIOD.

D) SOME DELEGATIONS STATED THAT A FLOOR PRICE MIGHT BE CONSIDERED ONE OF THE POINTS OF REFERENCE FOR THE ESTABLISHMENT OF AN EQUILIBRIUM PRICE. IN THIS CONNECTION LIMITED OFFICIAL USE
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SEVERAL DELEGATIONS SUGGESTED THAT ADDITIONAL REFERENCE POINTS FOR AN EQUILIBRIUM OF INTERESTS BETWEEN PRODUCERS AND CONSUMERS MIGHT BE:

-- A PRICE LEVEL AT WHICH OPEC SURPLUS MIGHT BE REDUCED TO ZERO IN THE LONG RUN BUT MIGHT BE NEGATIVE IN THE IMMEDIATE FUTURE;

-- A LEVEL WHICH WOULD MINIMIZE DISTORTIONS BOTH IN COUNTRIES WITH LARGE ENERGY DEVELOPMENT POTENTIAL AND IN COUNTRIES WHICH MIGHT SUPPLY CAPITAL TO EXPLOIT THE POTENTIAL IN THE FORMER COUNTRIES.

3. THE AMOUNT OF NEW ENERGY SUPPLIES WHICH MIGHT BE AVAILABLE AT DIFFERENT PRICE LEVELS AND THE TIME SCALE INVOLVED.

THE LEVEL OF A COMMON LEVEL OF PRICE PROTECTION SHOULD BE HIGH ENOUGH TO PROTECT NEW INVESTMENT IN A

LARGE PART OF CONVENTIONAL NUCLEAR AND FOSSIL FUEL SOURCES, BUT IT SHOULD NOT BE SO HIGH AS TO PROTECT HIGH COST MARGINAL RESOURCES. THE OBJECTIVE SHOULD BE TO REDUCE DOWNSIDE RISK TO A LEVEL AT WHICH IT DOES NOT INHIBIT INVESTMENT IN THESE ENERGY SOURCES WHICH WILL PROVIDE THE GREAT BULK OF NEW ENERGY OVER THE NEXT TEN YEARS. THIS WOULD IN ALL LIKELIHOOD BE A LEVEL SUBSTANTIALLY BELOW THE CURRENT WORLD PRICE BUT SIGNIFICANTLY ABOVE THE PRE-1973 PRICE.

IT WAS AGREED THAT ADDITIONAL ANALYTICAL WORK WAS NEEDED BEFORE A SPECIFIC PRICE COULD BE FIXED IF A GENERAL MEASURE OF PRICE PROTECTION IS AGREED UPON BY THE IEA. IN THIS CONNECTION THE CHAIRMAN URGED ALL DELEGATIONS TO PROVIDE THE AD HOC GROUP WITH COMPLETED QUESTIONNAIRES ON ALTERNATIVE SOURCES IN ORDER TO PERMIT PRELIMINARY ELABORATION OF AN IEA SUPPLY CURVE. DELEGATIONS WERE URGED TO GIVE PRIORITY ATTENTION TO NUCLEAR COSTS.

4. THE NEED TO TAKE INTO ACCOUNT THE RELATIONSHIP BETWEEN THE LEVEL OF OIL PRICES AND IEA CONSERVATION OBJECTIVES.

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TWEEN THE LEVEL OF OIL PRICES AND IEA CONSERVATION OBJECTIVES.

SEVERAL DELEGATIONS NOTED THAT IF OIL PRICES DECLINE SIGNIFICANTLY, THERE WOULD BE A NEGATIVE IMPACT ON THEIR CONSERVATION EFFORTS. OTHER DELEGATIONS REITERATED THEIR GOVERNMENTS INTENTION TO CARRY OUT CONSERVATION PROGRAMMES IRRESPECTIVE OF DEVELOPMENTS IN WORLD OIL PRICES. THIS CONSERVATION EFFORT WAS REGARDED BY SEVERAL DELEGATIONS AS A PART OF THEIR BURDEN, ESPECIALLY FOR THOSE COUNTRIES WITH LITTLE ENERGY POTENTIAL. IT WAS GENERALLY AGREED THAT THERE IS A NEED FOR SOME ASSURANCE THAT THE REDUCED IMPORT DEPENDENCE EFFECTS OF ACCELERATED DEVELOPMENT SHOULD NOT BE DAMAGED BY UNDUE RESTIMULATION OF DEMAND FOR IMPORTED OIL WHEN WORLD PRICES DECLINE.

5. A MEDIUM-TERM ANALYSIS OF OIL PRICES, INCLUDING THE CONCEPT OF AN EQUILIBRIUM PRICE.

WITH REGARD TO MEDIUM TERM ANALYSIS OF THE INTERNATIONAL OIL MARKET AND ITS POTENTIAL IMPLICATIONS FOR IEA PROGRAMS TO DEVELOP NEW ENERGY SUPPLIES, THE CHAIRMAN EXPRESSED HIS INTENTION TO CONSULTATIONS WITH THE CHAIRMAN OF THE SOM. THE US DELEGATION AGREED THAT IT

WOULD DRAFT A BRIEF PAPER ON THIS TOPIC TO BE CONSIDERED AT THE NEXT MEETING OF THE SLT.

6. TIMING

THE GOVERNING BOARD SHOULD ADDRESS THE QUESTION OF TIMING WITH REGARD TO THE ELABORATION OF SPECIFIC ELEMENTS OF A COORDINATED SYSTEM PARTICULARLY IN CONNECTION WITH THE FIXING OF A COMMON LEVEL OF PRICE PROTECTION. TWO DELEGATIONS SUGGESTED THAT IEA INTERESTS MIGHT BE ADEQUATELY SERVED BY ANNOUNCING IN ADVANCE OF A DIALOGUE WITH PRODUCERS OUR DELIMINATION TO TAKE APPROPRIATE ACTION (INCLUDING THE POSSIBILITY OF FIXING A COMMON LEVEL OF PRICE-PROTECTION) TO ACCELERATE DEVELOPMENT OF ALTERNATIVE SOURCES AND ARGUED THAT IEA LIMITED OFFICIAL USE
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CREDIBILITY AND THEREBY ITS BARGAINING POSITION COULD BE REINFORCED BY GIVING SOME ATTENTION TO THE MECHANISMS FOR UPHOLDING SUCH A LEVEL OF PROTECTION BEFORE ANNOUNCING ITS INTRODUCTION AND POSSIBLE LEVEL.

OTHER DELEGATIONS STATED THAT OUR POSITION WOULD BE CONSIDERABLY ENHANCED IF WE COULD REACH AGREEMENT NOW ON THE ACTUAL ELEMENTS OF OUR COORDINATED APPROACH, INCLUDING AGREEMENT TO APPLY A COMMON LEVEL OF PRICE PROTECTION--POSSIBLY WITHIN AN AGREED RANGE. THE TURKISH DELEGATION EXPRESSED THE VIEW THAT ANY MENTION OF SET FLOOR PRICES WOULD CAUSE A GENERAL TENDENCY TO INCREASE WORLD ENERGY PRICES AND ENCOURAGE INEFFICIENT INVESTORS WHILE ALSO JUSTIFYING OPEC PRICES. THIS DELEGATION MAINTAINED THAT ITS VIEWS ON THE FIRST PART OF THE SLT REPORT SHOULD BE TAKEN INTO CONSIDERATION IN THE SAME CONTEXT.

7. SHARING OF COSTS AND BENEFITS.

THE SLT HAD AN EXTENSIVE DISCUSSION OF THE NEED TO ASSURE THAT A COORDINATED SYSTEM TO ACCELERATE THE DEVELOPMENT OF ALTERNATIVE SOURCES OF ENERGY PROVIDES AN EQUITABLE BALANCE OF ADVANTAGE AMONG THE PARTICIPATING COUNTRIES. MOST DELEGATION AGREED THAT THIS ISSUE OF EQUITY SHOULD BE CONSIDERED IN TERMS OF THE SYSTEM AS A WHOLE AND NOT JUST IN TERMS OF INDIVIDUAL ELEMENTS OF THAT SYSTEM.

IT WAS GENERALLY AGREED THAT ALL PARTICIPATING COUNTRIES STAND TO RECEIVE CERTAIN BENEFITS FROM A COORDINATED SYSTEM WHICH ACCELERATES ALTERNATIVE SOURCES

BECAUSE OF ITS FAVORABLE IMPACT ON THE WORLD SUPPLY/ DEMAND BALANCE FOR OIL.

THOSE COUNTRIES WITH RELATIVELY LITTLE POTENTIAL TO DEVELOP FOSSIL FUELS AND WHO WILL CONTINUE TO IMPORT A SUBSTANTIAL PORTION OF THEIR ENERGY REQUIREMENT ARE CONCERNED THAT THEY NOT BE EXPECTED TO PAY TOO HIGH A PRICE IN STIMULATING THE DEVELOPMENT OF ALTERNATIVE LIMITED OFFICIAL USE LIMITED OFFICIAL USE

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SOURCES IN OTHER IEA COUNTRIES. UNDER THE COORDINATED SYSTEM OUTLINED ABOVE THE PRINCIPLE COST TO THESE FOSSIL FUEL DEFICIENT COUNTRIES WOULD BE FOREGOING THE ABILITY TO PASS DIRECTLY TO ENERGY-INTENSIVE INDUSTRIES AND TO CONSUMERS THE FULL BENEFITS OF A POSSIBLY SUBSTANTIAL FUTURE DROP IN WORLD OIL PRICES.

ON THE OTHER HAND, THOSE COUNTRIES WITH GREATER FOSSIL FUEL POTENTIAL, WHO WILL IN ALL LIKELIHOOD HAVE TO BEAR THE MAJOR CAPITAL AND OTHER COSTS OF DEVELOPING THIS ENERGY, ARE CONCERNED THAT A DECLINE IN WORLD OIL PRICES--BROUGHT ABOUT IN LARGE MEASURE BY THEIR ACCELERATED DEVELOPMENT PROGRAMS--WOULD LEAD TO THE IMPOSITION OF EXCESSIVE BURDENS ON THEIR ECONOMIES OR AN UNREASONABLE INCREASE IN CONSUMPTION OF LOWER PRICED IMPORTED OIL BY ENERGY DEFICIENT COUNTRIES, THUS NEGATING THE REDUCED IMPORT DEPENDENCE PROGRAM OF THE GROUP.

IT WAS NOTED THAT EVEN IF THE PRICE OF IMPORTED OIL FELL BELOW A COMMON LEVEL OF PROTECTION, IEA MEMBERS WOULD REMAIN FREE TO CAPTURE THE BALANCE OF PAYMENTS BENEFITS OF THESE LOWER WORLD PRICES. ALSO, WHILE THEY WOULD FOREGO THE POSSIBILITY OF PASSING THROUGH DIRECTLY TO THEIR ECONOMIES THE DIFFERENCE BETWEEN THE COMMON LEVEL OF PROTECTION AND THE IMPORTED COST, THEY WOULD IN MOST CASES BE FREE TO CAPTURE THESE ECONOMIC RENTS FISCALLY. IN ADDITION, THE FOSSIL FUEL DEFICIENT COUNTRIES DO HAVE THE POTENTIAL TO INVEST IN NUCLEAR POWER, AND SUCH INVESTMENT WOULD BE PROTECTED BY A COMMON IEA MEASURE OF PRICE PROTECTION.

SEVERAL DELEGATIONS NOTED THAT THERE IS A RELATIONSHIP BETWEEN THE POTENTIAL COSTS ENERGY DEFICIENT COUNTRIES MIGHT AGREE TO ASSUME UNDER A GENERAL MEASURE OF PRICE PROTECTION AND THEIR ABILITY TO PARTI-

CIPATE IN THE DEVELOPMENT OF ALTERNATIVE ENERGY UNDER A
COOPERATIVE APPROACH RELYING ON SPECIFIC MEASURES.

8. THE TURKISH DELEGATION EXPLAINED THE SITUATION IN
COUNTRIES WITH LOW PRICE ENERGY RESOURCES REGARDING THE
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POSSIBLE INEQUITY OF SHARING OF COSTS AND BENEFITS
AND GENERAL BURDEN SHARING WHICH WOULD RESULT IN INVEST-
ING HEAVILY ON THESE RESOURCES AND NOT BEING ABLE TO
BENEFIT FROM THE ECONOMICS OF SUCH INVESTMENT IF A
FLOOR PRICE WOULD BE ADOPTED. KISSINGER

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